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IN THE

Supreme Court of the United States

OCTOBER TERM, 1974

No. 74-626

CONTINENTAL ILLINOIS NATIONAL BANK AND TRUST COMPANY OF CHICAGO,
Petitioner,

vs.

HAROLD G. O'BRIEN, ET AL.,
Respondents,

and

RELATED CASES

BRIEF IN OPPOSITION TO PETITION FOR CERTIORARI

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Respondents pray that the Petition for Writ of Certiorari be denied.

OPINIONS BELOW

The unpublished order of the Court of Appeals for the Seventh Circuit of which review is sought is reproduced at page A1 of Petitioner's Appendix. The unpublished order of the Court of Appeals denying a petition for rehearing with suggestion for rehearing *en banc* is reproduced at page A25 of

Respondents' Appendix.[1] The order of the district court denying petitioner's motion to dismiss these six cases, reported at CCH Fed.Sec.L.Rep. ¶ 94,565 (May 10, 1974), is reproduced at page A2 of Petitioner's Appendix. The unpublished order of the district court (July 8, 1974) denying petitioner's motion for interlocutory appeal pursuant to 28 U.S.C. § 1292(b) is reproduced at page A26 of Respondents' Appendix.

QUESTION PRESENTED

Whether, in a private action for damages against a national bank under the antifraud provisions of the federal securities laws, an order denying a motion for reference of but one of multiple claims to the Comptroller of the Currency under the doctrine of primary jurisdiction is appealable under 28 U.S.C. § 1291.[2]

1. The denial of the petition and suggestion for rehearing *en banc* indicates that six of the seven circuit judges (Judge Cummings not sitting) in active service in the Seventh Circuit did not consider the proceedings below as involving a question of exceptional importance or that consideration by the full court of the question involved was necessary to secure or maintain uniformity of its decisions. See F.R.A.P. Rule 35(a), (b), 28 U.S.C.A.

2. The logical extension of this question involves the appealability *as a matter of right* of every order denying reference to a regulatory agency sought under the doctrine of primary jurisdiction. If petitioner's position that every such order is appealable as of right is sustained, the impact on courts of appeals, already burdened with overcrowded dockets, would be overwhelming. Given the myriad federal agencies, one or more of which has some form of regulatory jurisdiction over at least one area of interstate commerce, piecemeal appeals would tax the appellate process beyond its present limits.

STATEMENT OF THE CASE

These six cases all are brought in part under the antifraud provisions of the federal securities laws.[3]

Plaintiffs in each of these cases are, with few exceptions, trustees of employee benefit plans, including pension funds.[4]

The operative facts alleged in each of the complaints are substantially identical. In each of these cases the plaintiffs appointed defendant bank as their fiduciary agent or trustee with discretion to select, purchase, hold and sell securities suitable for trust investment.

In each complaint the bank is charged with investing assets of plaintiffs' fund in securities of an issuer with which defendant bank had, at the same time, a substantial but undisclosed, creditor and "insider" relationship. It is alleged that, in connection with the securities transactions complained of, defendant bank concealed from plaintiffs the material facts respecting its creditor relationship.[5]

3. All of the cases are brought under Section 10(b) of the Securities Exchange Act of 1934, 15 U.S.C. § 78j(b). *O'Donnell* is also brought under § 17a of the Securities Exchange Act of 1933, 15 U.S.C. § 77g(a). Based on the same facts alleged in the statutory counts, all of the complaints also plead common law claims for breach of trust and contract, under the doctrine of pendent jurisdiction.

4. In all cases, plaintiffs are markedly different from the "contingent beneficiaries and remaindermen" alluded to at the end of the footnote at Pet. 5. The true relationship between plaintiffs, as *investors,* and defendant, as *an active money manager,* was aptly recognized by the district court in its decision of May 10, 1974. Pet. App. A9.

5. Petitioner isolates this claim and urges the *in terrorem* argument that, if it is enforced, major banks would be crippled. (Pet. p. 4n**). Such predictions of "disaster to business" are not unfamiliar. Virtually the identical argument was rejected by this Court more than 70 years ago in construing another broad remedial

It is further alleged that defendant bank concealed from plaintiffs the fact that their investments in the subject securities were rendered illiquid because of defendant bank's "insider" position, which inhibited or prohibited its trading in such securities.

Plaintiffs further charge that, because of these concealed conflicts, and notwithstanding defendant's fiduciary duty to liquidate said investments when continued retention became imprudent, defendant delayed and postponed such liquidation in order to favor and protect its own interests over those of plaintiffs.

Plaintiffs further allege that, based on its analysis of the financial condition of the issuer, defendant bank knew but failed to disclose to plaintiffs that the subject securities were not of suitable investment quality for plaintiffs' pension funds, and that defendant concealed such information from plaintiffs from the time the subject securities were purchased to and including the time of sale thereof.[6]

Petitioner moved to dismiss these cases on the grounds, among others, that (a) the complaints failed to state a claim

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statute. *Northern Securities Co.* v. *United States*, 193 U.S. 197, 351-352 (1904). The same argument, twice advanced below, failed to impress let alone terrify either the district court or the Court of Appeals. In any case, it is totally extraneous to the question of appealability. Assuming *arguendo* that it has any merit at all, the argument should be directed to Congress, not the judiciary. It raises policy questions "which belong to another department." *Id.*

6. Defendant's answer in *Vest* which, pursuant to Rule 9(a) of the General Rules of the District Court, also contains a complete restatement of the allegations in the complaint, is reproduced in Respondents' Appendix at p. A1. The allegations in this complaint are typical of those in all of the cases, differing in substance only with respect to the identity of the securities involved, the dates and amounts of purchases and sales and the loss incurred. See, *e.g.*, the complaints in *O'Brien*, No. 72C 2551, and *O'Donnell*, No. 73C 772, included in the record certified to this Court by the Clerk of the District Court.

upon which relief can be granted; (b) the court lacked jurisdiction over the subject matter; (c) national banks, when acting as trustees, are impliedly exempt from the antifraud provisions of the federal securities laws; and (d) the Comptroller of the Currency had *exclusive* jurisdiction of the claims asserted. The district court rejected these grounds and denied petitioner's motions. (Pet. App. A2) In ruling on the last ground mentioned, the district court stated that it agreed with the petitioner's concession that the doctrine of *primary* jurisdiction was inapplicable to respondents' Rule 10b-5 claims. (Pet. App. 14)

Subsequently, petitioner moved for reconsideration of this order and, for the first time, invoked the doctrine of primary jurisdiction for the purpose of seeking a stay of proceedings pending a reference of one of the issues in these cases to the Comptroller of the Currency.[7] The district court also denied this motion.

Thereafter petitioner first moved to amend the district court's order to permit interlocutory appeal under 28 U.S.C. § 1292(b). After this motion was denied (Resp. App. A25), petitioner nevertheless sought to appeal *as of right* under 28 U.S.C. § 1291 from the district court's aforesaid orders. Petitioner's attempt to so appeal was rejected by the court below on the ground that the orders appealed from were "not final or otherwise appealable." (Pet. App. A1)

The court below did not consider or decide the correctness of the orders from which appeal was sought, notwithstanding

7. Petitioner's position in this Court, as it was below, is that the sole claim it seeks to have referred to the Comptroller is its alleged conflict of interest arising out of its creditor relationship with an issuer whose equity securities it acquired for plaintiffs' accounts. (Pet. p. 4) As noted above, this claim is but one of numerous statutory and common law claims asserted in the complaints; petitioner does not argue here that the doctrine of primary jurisdiction is applicable to any of these other claims.

petitioner's efforts to persuade the court to consider the merits of the orders appealed from along with the question of their appealability.[8]

8. Although the merits of the district court's order denying a reference under the doctrine of primary jurisdiction are not before this Court and argument thereon is questionable (Cf. *Irvine* v. *California*, 347 U.S. 128, 129 (1954)), a considerable portion of the petition is devoted to just such an argument (Pet. 4-6, 7n, 12, 13n). Even so, petitioner's argument is highly dubious. The present cases present no conflict between regulatory statutes, a specific requirement in *Ricci* v. *Chicago Mercantile Exchange*, 409 U.S. 289 (1973). Nor is the Comptroller of the Currency an agency whose functions "appear to encompass adjudication of the kind of substantive claims" made in these cases under the federal securities laws, *Chicago Mercantile Exchange* v. *Deaktor*, 414 U.S. 113, ..., 38 L.Ed.2d 344, 347 (1973). The notion that the Comptroller should adjudicate claims arising under regulations promulgated by the Securities and Exchange Commission is highly novel. Petitioner's suggestion that enforcement of the antifraud provisions of the federal securities laws is inimical to the conduct of a banking business under the national banking laws totally ignores this Court's consistent application of Section 10(b) of the 1934 Act to national banks in both their commercial and trust department activities without deference to any administrative agency. *Superintendent of Insurance* v. *Bankers Life & Casualty Co.*, 404 U.S. 6 (1971); *Affiliated Ute Citizens* v. *United States*, 406 U.S. 128 (1972). And see *James* v. *Gerber Products Co.* 483 F.2d 944 (6th Cir. 1973); *Leheigh Valley Trust Co.* v. *Central National Bank of Jacksonville*, 409 F.2d 989 (5th Cir. 1969); *Carroll* v. *First National Bank of Lincolnwood*, 413 F.2d 353 (7th Cir. 1969). Certainly if the primary jurisdiction issue were as omnipresent as petitioner urges here, the issue would have been raised by counsel in these cases or by the courts *sua sponte*.

REASONS FOR DENYING THE WRIT

The petition should be denied because: (a) the decision of the Seventh Circuit is not in conflict but is in accord with controlling decisions of this Court; and (b) the decision of the Seventh Circuit is not in conflict but is consonant with other decisions of courts of appeals on the same matter; assuming, *arguendo*, the existence of differences, they are not of such importance as to justify the issuance of the writ sought.

I.

THE RULING BELOW IS IN ACCORD WITH THE CONTROLLING DECISIONS OF THIS COURT

The petition relies primarily on this Court's seminal decision in *Cohen* v. *Beneficial Loan Corp.*, 337 U.S. 541 (1949) and asserts that the ruling of the court below conflicts with *Cohen* and with two later decisions of this Court applying its doctrine, *Eisen* v. *Carlisle and Jacquelin*, ... U.S. ....., 94 S.Ct. 2140, 40 L.Ed.2d 732 (1974), and *Local 438 Construction and General Laborers' Union* v. *Curry*, 371 U.S. 542 (1963). There is no such conflict.

A. Cohen Applies Only Where There Is a Showing of Irreparable Injury Because of the Ineffectiveness of Later Review

In *Cohen*, this Court held appealable "that small class [of decisions] which finally determine claims of right separable from, and collateral to, rights asserted in the action, too important to be denied review and too independent of the cause itself to require that appellate consideration be deferred until the whole case is adjudicated." 337 U.S. at 546.

The petition focuses on but one of *Cohen's* requirements: that the order for which appellate review is sought adjudicate a collateral claim. This emphasis is quite evident in petitioner's statement of the question presented, "whether the district court's refusal to refer or to stay is separate from and collateral to the merits of the cases and *therefore* appealable as a final order under 28 U.S.C. § 1291." (Pet. 3, emphasis added)

Petitioner all but ignores the most essential if not the controlling requirement in *Cohen*: that denial of immediate review would result in irremediable injury in that appellate review at a later date would be an "empty rite." *Swift & Co.* v. *Compania Colombiana Del Caribe,* 339 U.S. 684, 688-689 (1950); *Cohen* v. *Beneficial Loan Corp., supra* at p. 546; *Sears Roebuck & Co.* v. *Mackey,* 351 U.S. 427, 441 (1956).

In discussing this essential aspect of *Cohen,* Mr. Justice Jackson pointedly noted that when the time came to review a final judgment on the merits, "it will be too late effectively to review the present order and the rights conferred by the statute, if it is applicable, will have been lost, probably irreparably." 337 U.S. at 546. The lower courts and leading commentators have considered this irreparable injury feature of the *Cohen* doctrine to be decisive. See *e.g., United States* v. *Wood,* 295 F.2d 772, 777-78 (5th Cir. 1961); Note, *Appealability In The Federal Courts,* 75 *Harv.L.Rev.,* 351, 364 (1961).

Petitioner makes no showing whatsoever that if denied immediate review it will suffer the type of irreparable loss of rights contemplated in the cases upon which it relies. Instead, it claims some vague injury "in terms of wasted judicial resources" and "cost to the parties here involved." (Pet. 13) Avoiding the cost of protracted and potentially unnecessary litigation is not ground for holding an otherwise interlocutory order appealable. *Parr* v. *United States,* 351 U.S. 513, 519-20 (1956); *Cobbledick* v. *United States,* 309 U.S. 323 (1940).[9]

9. There is no case which holds that appeal of right is to be determined solely upon considerations of judicial economy. If so, by *reductio ad absurdum,* the denial of every motion to dismiss would be appealable as of right.

In *Cohen*, denial of immediate review would have compelled the defendant to litigate without the protection of security for costs, and reversal on later appeal would have afforded defendant only the meaningless opportunity to recover its costs against a possibly uncollectible defendant. This would have been as much an "empty rite" as affording the successful plaintiff in *Swift & Co., supra*, the privilege of attempting to attach a ship that had sailed. (339 U.S. at 689) Similarly, in *Eisen* v. *Carlisle and Jacquelin, supra*, denial of immediate review would irreparably injure defendants since they would be required to expend substantial funds for a class notice with a later appeal, if successful, affording them the dubious privilege of attempting to collect those costs from a plaintiff with a mere $70.00 interest in the case. Here, petitioner does not even suggest that, if denied immediate review, it might be unable to recover its proper costs after a successful trial on the merits.

Petitioner's inability to show any irreparable loss of rights quite obviously stems from the fact that the district court's orders can be effectively reviewed after judgment on the merits. Two circuits have specifically so held. *Thill Securities Corp.* v. *New York Stock Exchange*, 469 F.2d 14, 17 (7th Cir. 1972); *American Airlines, Inc.* v. *Forman*, 204 F.2d 230, 232 (3d Cir. 1953). Of course, should defendant prevail on the merits, the entire primary jurisdiction issue would be mooted, or conceivably it could be raised by defendant in the event of an appeal by plaintiff.

Restating its principal argument that immediate review is necessary to avoid a needless trial, petitioner also urges that "the order appealed from is 'fundamental' to further proceedings in the Court below" (Pet. pp. 12-13), relying on *Gillespie* v. *U.S. Steel Corp.*, 379 U.S. 148 (1964). This contention derives from a severely truncated description of the complaints, reducing them to but a single statutory claim for concealment of a conflict of interest. (Pet. p. 4) But the complaints also allege many statutory and pendent common law claims

founded on wholly independent facts,[10] none of which claims are asserted by petitioner to be within the primary jurisdiction of the Comptroller, and all of which, concededly, must therefore proceed through discovery, pretrial and trial as in any other lawsuit.

Thus, even if the single conflict of interest claim isolated by petitioner were to be referred to the Comptroller, and even if the Comptroller were to express an opinion so persuasive as to result in its dismissal, the effect on the expense and duration of trial of the remaining claims would be insignificant.[11]

B. Petitioner's Claim of a Right to a Reference to the Comptroller Under the Doctrine of Primary Jurisdiction Is Not Separable from and Collateral to Rights Asserted in These Actions

An additional essential feature of *Cohen* is that the order sought to be appealed must finally determine claims of right *separable from and collateral to* rights asserted in the action. *Cohen* v. *Beneficial Loan Corp., supra,* at 546 (emphasis added). Petitioner would satisfy this requirement with no more than a chain of *ex cathedra* pronouncements. (Pet. 11-12)

The issue of collateralness requires an analysis of the possible effect of an ultimate appeal on a judgment in plaintiffs' favor. The question is whether, after judgment on the merits, a reversal

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10. See Statement of the Case, p. 4, *supra,* and *Vest* complaint, which is typical, (incorporated in Defendant's Answer, Resp. App. A1, A5, A7-10).

11. For these reasons, *inter alia, Gillespie* is inapposite, and petitioner's predictions of wasted judicial resources and needless expense (Pet. pp. 8, 13) are without merit. In any event, it must be recognized that *Gillespie* was considered by this Court to be an "obviously marginal case", involving a number of unusual circumstances, including the agreement by both the petitioner and respondent that the appeal should be heard as of right. The Court itself seems to have regarded the case as *sui generis* and limited to the peculiar circumstances there present. (379 U.S. at 154)

of the interim order would necessarily leave the judgment untouched. In *Cohen, supra, Swift & Co., supra* or *Eisen, supra,* for example, if plaintiff obtained a judgment on the merits, a subsequent holding by a court of appeals that the disputed interim order was erroneously entered would have no effect on plaintiff's judgment. Conversely, in the present cases, if, on review after judgment on the merits for plaintiffs the Court of Appeals should reverse the order denying reference to the Comptroller, plaintiffs' judgment would in all probability be affected. At the very least, the judgment would be stayed; at most, after reference to the agency, the judgment would be subject to modification or vacation, depending upon what findings or opinions, if any, were expressed by the Comptroller, and the weight which the court thereafter gave them. Cf. *Thill Securities Corp.* v. *New York Stock Exchange, supra,* and *American Airlines, Inc.* v. *Forman, supra.*

Furthermore, it is apparent that the district court's denial of petitioner's motion for reference to the Comptroller was an adjudication not of a collateral issue but of a claim touching upon the merits of plaintiffs' claims. In denying petitioner's motion for certification under 28 U.S.C. § 1292(b) the district judge stated:

> "Implicit in this motion is the contention that if the Comptroller of the Currency were to find that no conflict of interest existed under the national trust regulations, 12 C.F.R. 9.12, a 10b-5 action could not be maintained. As this Court noted in its prior opinion (pp. 18-19, May 10, 1974), such clearly was not the intendment of the trust regulations, see *Blaney* v. *Florida Nat'l Bank at Orlando,* 357 F.2d 27, 30 (5th Cir. 1966). A 10b-5 claim, as well as a common law cause of action for breach of fiduciary duties, will lie regardless of any determination by the Comptroller." (Resp. App., p. A27)

In short, the district court, in a real sense, was ruling on the relevancy of defenses asserted on the merits of respondent's

claims, a ruling which necessarily was a "[step] towards final judgment." *Cohen, supra,* at 546.[12]

Petitioner's reliance on *Local 438 Construction and General Laborer's Union* v. *Curry,* 371 U.S. 542 (1963) is misplaced. In *Curry* the Court was not dealing with a simple question of routing as between two tribunals each having jurisdiction. Rather, the Court was reviewing, in the very special area of state-federal contact, an order by a tribunal totally without power to consider the merits, jurisdiction having been preempted by Congress' adoption of a uniform national labor policy. In that case, the Court granted review of a state court injunction in a labor dispute, despite the argument that, since the injunction was temporary rather than permanent, the order was not "final," within the meaning of 28 U.S.C. § 1257.

In permitting review, the Court emphasized that "postponing review would seriously erode the national labor policy requiring the subject matter of respondents' cause to be heard by the National Labor Relations Board, not by the state courts" and recognized that "authorizing the issuance of a temporary injunction, as is frequently true of temporary injunctions in labor disputes, may effectively dispose of petitioner's rights and render entirely illusory his right to review here as well as his right to a hearing before the National Labor Relations Board." (371 U.S. at 550) The state court, as this Court found, did not have, and could never have had, jurisdiction. Thus petitioner's *ipse dixit,* that the fact that *Curry* involved *exclusive* rather than *primary* jurisdiction makes no difference (Pet. p. 10), is fallacious; the difference is crucial.

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12. The correctness of the district court's ruling is amply supported by this Court's decision in *SEC* v. *Capital Gains Research Bureau, Inc.,* 375 U.S. 180 (1963). The existence of the conflict of interest and its potential for abuse are to be judged by the *investor,* not by the court, and certainly not by a federal agency. 375 U.S. at 196. The fiduciary's good faith, lack of intent to injure, the absence of evidence that the judgment of the fiduciary was intrinsically unsound or corrupted by self-interest, and lack of injury in fact are all immaterial. *Id.* at 184-85, 200-01.

The question of finality in *Curry* as well as in *Mercantile National Bank* v. *Langdeau*, 371 U.S. 555 (1963), also cited by petitioner, was decided under 28 U.S. § 1257. These decisions should not "be regarded as controlling the very different question of what is a 'final decision' under 28 U.S.C. § 1291." 9 Moore, *Fed. Prac.* ¶ 110.10, pp. 136-37 (2d ed. 1973).[13]

II.

THE RULING BELOW HOLDING THAT THE ORDERS APPEALED FROM WERE NOT FINAL OR OTHERWISE APPEALABLE IS CONSONANT WITH THE DECISIONS OF OTHER CIRCUITS

Petitioner argues, as a ground for granting the writ, that it is necessary for this Court to resolve a conflict between the Second and Seventh Circuit Courts of Appeals. This conflict is claimed to exist between the ruling of the court below in the present cases, adhering to its earlier ruling in *Thill Securities Corp.* v. *New York Stock Exchange*, 469 F.2d 14 (7th Cir. 1972), on the one hand and the ruling of the Second Circuit in *CAB* v. *Aeromatic Travel Corp.*, 489 F.2d 251 (2nd Cir. 1974) on the other. In both the present cases and in *Thill*, a district court order denying a motion for reference to an agency sought on the ground of primary jurisdiction was held to be not a final order and therefore not appealable. The Third Circuit's holding in *American Airlines, Inc.* v. *Forman*, 204 F.2d

13. Professor Moore's explanation is worth noting:

> "In construing § 1257, the Court is confronted with a very rigid requirement of finality untempered by the many devices for interlocutory review available in the federal system. The same considerations that led to the creation of those devices support a very liberal interpretation of 'final' as the term is used in § 1257, but the availability of the devices in the federal system makes an identically liberal interpretation of 'final' as the term is used in § 1291 both unnecessary and undesirable."

Otherwise, *Curry* and *Langdeau* would stand for the proposition that every order denying a motion to dismiss for lack of jurisdiction would be final and appealable under 28 U.S.C. § 1291.

230 (3rd Cir. 1953) is in accord. Both *Thill* and *American Airlines* held that effective review of the disputed order was available on appeal after final judgment. (*Thill, supra* at 17; *American Airlines, Inc., supra,* at 232)

Aeromatic Travel was an action brought by the Civil Aeronautics Board seeking immediate injunctive relief to enjoin defendant from further violation of that agency's regulations. On defendant's motion the district court stayed the proceedings and referred the case to the agency, *which was itself the plaintiff,* on the ground of primary jurisdiction.

The effect of the entry of this order was to permit the allegedly unlawful conduct of the defendant to continue while administrative proceedings were conducted. In concluding that later review would be ineffective, the Second Circuit noted that Congress provided for direct enforcement of the Federal Aviation Act and the Board's regulations by suit in the district court for the "obvious purpose" of assuring "speedy enforcement of the Act." The two-year delay resulting from the district court's order "clearly thwarted this [Congressional] purpose." 489 F.2d at 254.

In contrast, had the district court there *denied* the motion for referral to the agency, that order, like the order in the present cases, would not have been appealable, for "in such a situation the rights of all the parties can be adequately protected while the litigation on the main claim proceeds." *Swift & Co., supra,* at 689.

Considering the criteria of *Cohen, Swift* and *Eisen,* requiring irremediable injury and ineffectiveness of later review, there is no conflict between the Second Circuit's opinion in *Aeromatic Travel* on the one hand, and *Thill, American Airlines* and the present cases on the other.

However, by focusing solely upon the Second Circuit's statement that the district court's order was *collateral,* petitioner would create a conflict on this ground alone. But even if

Aeromatic is correct and *Thill* is incorrect on the "collateral" question, both opinions nevertheless correctly apply the *Cohen* doctrine. The Seventh Circuit's presumed departure from *Cohen*, holding that the disputed order did not decide a collateral question, becomes immaterial in view of its correct conclusion with respect to the effectiveness of later review after judgment on the merits. Thus the conflict, immaterial as it was to the ultimate decision in *Thill*, would not be so "real and embarrassing" as would warrant granting the writ. *Layne & Bowler Corp.* v. *Western Well Works, Inc.*, 261 U.S. 387, 393 (1923).[14]

14. Petitioner also criticizes the court below for inconsistency in its basic approach to the questions here involved, citing *Drexler* v. *Southwest Dubois School Corp.*, ... F.2d ....., No. 72-1918 (Oct. 15, 1974), (Pet. p. 8n). *Drexler*, however, is not based on *Cohen*. It involved the doctrine of federal abstension, and the Seventh Circuit's holding there was expressly based on this Court's decision in *Idlewild Bon Voyage Liquor Corp.* v. *Epstein*, 370 U.S. 713, 715n.2 (1962), recognizing the appealability of lower court abstention orders: upon entry of such on order "appellant is effectively out of court." (*Id.*) Petitioner's criticism is unwarranted.

CONCLUSION

This Court should deny the petition for certiorari in these cases because the decision of the Seventh Circuit below is in conformity with the controlling decisions of this Court, and because there is no conflict between the decision below and those of other circuits.

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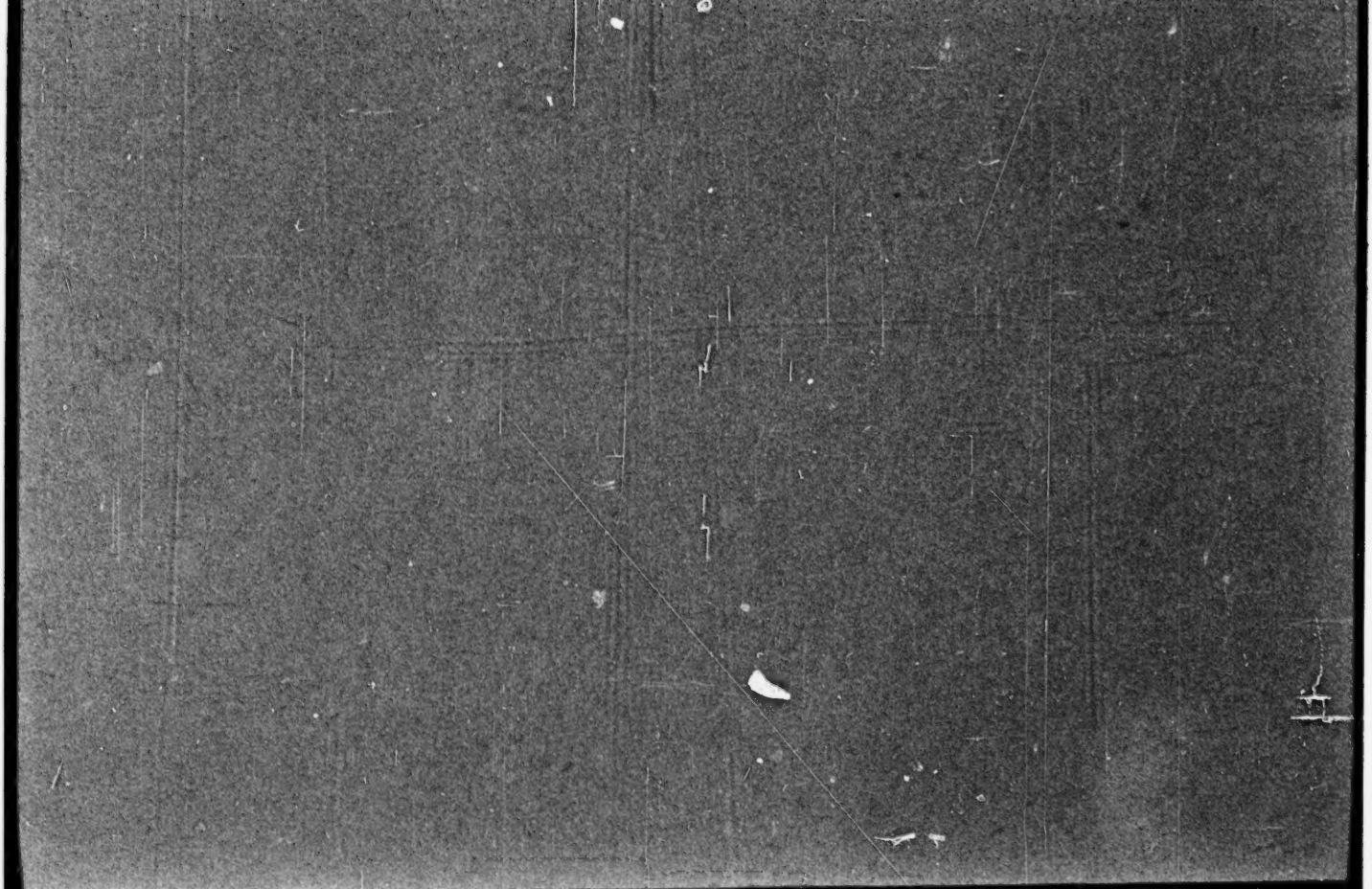
Appendix



APPENDIX

George Vest, Jr., Charles A. Thompson, Milton Holzman, Richard S. Pepper, Jack H. Paschen, and Herbert S. Church, Jr. as Trustees of the Chicago District Council of Carpenters Pension Fund v. Continental Illinois National Bank and Trust Company of Chicago, a National Banking Association.

United States District Court, Northern District of Illinois, Eastern Division. No. 72 C 2935.

ANSWER

Now comes Defendant, Continental Illinois National Bank and Trust Company of Chicago, a National Banking Association, (hereinafter referred to as Continental Bank), by its attorneys, Miles G. Seeley and Bryson P. Burnham, and in answer to Plaintiffs' Amended Complaint, alleges and states as follows:

COUNT I

1. Paragraph 1 of Count I of the Amended Complaint reads:

> "1. This action is brought under Section 10(b) of the Securities Exchange Act of 1934 (15 USC 78j) and Rule 10b-5 thereunder. This Court has jurisdiction of this action under Section 27 of said Act (15 USC 78 aa)."

1. Continental Bank admits that this action purports to be brought under the statute and rule referred to, but denies that Plaintiff has any cause of action thereunder. Continental Bank admits that if this action were properly brought under said statute and rule, this Court would have jurisdiction under the statute referred to in the last sentence of paragraph 1 of Count I of the Amended Complaint.

2. Paragraph 2 of Count I of the Amended Complaint reads:

> "2. Plaintiffs George Vest, Jr., Charles A. Thompson, Milton Holzman, Richard S. Pepper, Jack H. Paschen and Herbert S. Church, Jr. (hereinafter referred to as 'Plaintiffs' or 'Trustees') are the Trustees of the Chicago District Council of Carpenters Pension Fund, a trust organized under the laws of the State of Illinois for the benefit of carpenters employed in the Greater Chicago area."

2. Continental Bank is informed and believes that the allegations contained in paragraph 2 of Count I of the Amended Complaint are true.

3. Paragraph 3 of Count I of the Amended Complaint reads:

> "3. Defendant Continental Illinois National Bank and Trust Company of Chicago ('Continental') is a national banking association with its principal place of business in Chicago, Illinois."

3. Continental Bank admits the allegations contained in paragraph 3 of Count I of the Amended Complaint.

4. Paragraph 4 of Count I of the Amended Complaint reads:

> "4. At all times material herein there was in force and effect an agreement between the Trustees of the Carpenters Pension Fund and Continental pursuant to which Continental was appointed and agreed to act as agent for the Trustees with respect to investment of funds deposited by them with Continental. Under said agreement the Trustees authorized Continental, in the latter's discretion, to select and purchase securities out of said deposited funds. At all times material herein Continental, pursuant to said contract, had a fiduciary duty to the Trustees to exercise such discretion with prudence and with due regard for the safety of the capital of the Carpenters Pension Fund."

4. Continental Bank admits that there was, at all times material herein, an agreement between it and the Trustees of

the Chicago District Council of Carpenters Pension Fund (hereinafter referred to as Carpenters) pursuant to which Continental Bank was appointed to act as "Agent" for Carpenters with respect to investment of funds deposited by Carpenters with Continental Bank. Continental Bank admits that under said agreement, Continental Bank had discretion within certain written guidelines to select and purchase securities out of said deposited funds. Continental Bank admits that the relationship between it and the Trustees of Carpenters was in part fiduciary in nature but denies that the allegations of paragraph 4 of Count I of the Amended Complaint accurately characterize the standard for the investment of funds as set forth in the agreement between the parties thereto.

5. Paragraph 5 of Count I of the Amended Complaint reads:

> "5. Between August 19, 1966 and November 16, 1966, pursuant to the authority granted it by the Trustees under the aforesaid agency agreement, Continental purchased a total of 6,000 shares of Management Assistance, Inc. ('MAI') common stock for the account of the Carpenters Pension Fund for a total price of $147,050. At the time of such purchases, MAI was principally engaged in the purchase and leaseback of used computers and other data processing equipment. The price-earnings multiple for the shares purchased was approximately 50."

5. Continental Bank admits the allegations contained in paragraph 5 of Count I of the Amended Complaint, except that it states that the total price of the 6,000 shares of MAI stock was $148,250 and that the price-earnings multiple for the shares purchased was approximately 42.

6. Paragraph 6 of Count I of the Amended Complaint reads:

> "6. At all times material herein the common stock of MAI was traded in the over-the-counter market. The aforesaid purchases of MAI common stock were effected through the use of the United States mails and through instrumentalities of interstate commerce."

6. Continental Bank admits the allegations of paragraph 6 of Count I of the Amended Complaint.

7. Paragraph 7 of Count I of the Amended Complaint reads:

> "7. At the time of each of the aforesaid securities purchases by Continental, said bank was the principal creditor of MAI, having loaned or agreed to loan to MAI or to one or more of its subsidiaries the sum of $65,000,000. At said time substantially all of the computers and other data processing equipment then owned by MAI was pledged to Continental to secure said indebtedness, and, in addition, to further secure such indebtedness, Continental had obtained the right to control MAI's future dividend payments and future borrowing rights."

7. Continental Bank denies the allegations of paragraph 7 of Count I of the Amended Complaint, except that Continental Bank states that MAI's dividend policy was restricted in that its loan agreement with Continental Bank provided that MAI would pay no dividends if, after giving effect to such a transaction, the outstanding indebtedness (excluding subordinated debt) of MAI would exceed 350% of MAI's consolidated net worth. Continental Bank further states that it agreed to assume the lead role among a group of participating banks and that said group agreed to loan MAI $65,000,000, and MAI pledged certain computers and data processing equipment to that group of participating banks, including Continental Bank, to secure said indebtedness.

8. Paragraph 8 of Count I of the Amended Complaint reads:

> "8. At said time Continental had, or had available to it, detailed inside information, with respect to the financial condition of MAI and its subsidiaries, including but not limited to, operating statements, balance sheets, cash flow schedules, and other information not then available to the investing public."

8. Continental Bank denies the allegations of paragraph 8 of Count I of the Amended Complaint, except it admits that

as a senior secured creditor of MAI it received certain MAI financial information more detailed than that available to the investing public, but it denies that those officers responsible for making investment decisions with respect to plaintiffs' funds had, or had available to them, such information for their use in making such decisions.

9. Paragraph 9 of Count I of the Amended Complaint reads:

> "9. At the time of said purchases Continental failed to disclose to Plaintiffs that it had a conflict of interest with Plaintiffs with a potential for abuse arising from the fact that Continental was then the principal creditor of the issuer of the aforesaid securities, and controlled the issuer's dividend payment and borrowing policies."

9. Continental Bank denies the allegations of paragraph 9 of Count I of the Amended Complaint, further denies that it had a conflict of interest as alleged, and therefore denies that it should have "disclosed" such matter to Plaintiffs.

10. Paragraph 10 of Count I of the Amended Complaint reads:

> "10. At the time of said purchases, Continental failed to disclose to Plaintiffs that it had and would continue to acquire inside information about MAI's affairs; that as an 'insider' it was or might be inhibited by law from trading in MAI stock; and that this inhibition was or might be in conflict with its aforesaid fiduciary duty to plaintiffs, with respect to its investment in MAI stock."

10. Continental Bank denies the allegations of paragraph 10 of Count I of the Amended Complaint, and therefore denies that it should have "disclosed" any of such matters to Plaintiff.

11. Paragraph 11 of Count I of the Amended Complaint reads:

> "11. Relying on Continental as a fiduciary, and having no knowledge of the material information concealed by Continental, as aforesaid, the plaintiff Trustees acquiesced in the investment of assets of the Carpenters Pension Fund by Continental in MAI securities, and continued so to

acquiesce until the sale of said securities. Because of said concealment, the Trustees were induced to continue their relationship with Continental and were induced not to invoke their power to terminate the aforesaid contractual relationship."

11. Continental Bank denies the allegations of paragraph 11 of Count I of the Amended Complaint, except it admits that the Plaintiffs acquiesced in the investment of their funds by Continental Bank in MAI securities, and continued so to acquiesce until the sale of said securities. Continental Bank further states that Carpenters terminated its relationship with Continental Bank on September 9, 1972.

12. Paragraph 12 of Count I of the Amended Complaint reads:

"12. In November and December, 1970, and June, 1971, Continental sold the 6,000 shares of MAI common stock purchased and held by it for the account of the Carpenters Pension Fund for a net consideration of $6,562.50."

12. Continental Bank admits the allegations of paragraph 12 of Count I of the Amended Complaint, and further states that Carpenters had previously received (on or about September 27, 1967) an additional $1,200.00 for a sale of rights to purchase MAI common stock.

13. Paragraph 13 of Count I of the Amended Complaint reads:

"13. As a result of the aforesaid conduct of Continental, Carpenters Pension Fund suffered a loss in the amount of $140,488.50, or approximately 95% of its total investment in MAI stock."

13. Continental Bank denies the allegations of paragraph 13 of Count I of the Amended Complaint.

14. Paragraph 14 of Count I of the Amended Complaint reads:

"14. The plaintiff Trustees had no knowledge of the aforesaid undisclosed material information until sometime

after Continental commenced selling the MAI common stock purchased and held by it for the account of the Carpenters Pension Fund."

14. Continental Bank denies the allegations of paragraph 14 of Count I of the Amended Complaint.

15. Paragraph 15 of Count I of the Amended Complaint reads:

"15. The aforesaid conduct of Continental was a violation of Section 10(b) of the Securities Exchange Act of 1934 and Rule 10b-5 thereunder."

15. Continental Bank denies the allegations of paragraph 15 of Count I of the Amended Complaint.

COUNT II

1.-6. Paragraphs 1-6 of Count II of the Amended Complaint reads:

"1.-6. Plaintiffs adopt and reallege as if the same were set forth here in full the allegations in paragraphs 1 through 6, both inclusive, of Count I hereof."

1.-6. Continental Bank adopts and realleges, as though the same were set forth here in full, its answers to paragraphs 1 through 6, both inclusive, of Count I of the Amended Complaint as its answers to paragraphs 1 through 6, both inclusive, of Count II of the Amended Complaint.

7. Paragraph 7 of Count II of the Amended Complaint reads:

"7. At the time of each of the aforesaid securities purchases by Continental, or prior thereto, Continental had, or had available to it, detailed information with respect to the financial condition of MAI including, but not limited to, operating statements, balance sheets, cash flow schedules, and other information which permitted Continental, by reason of the investment analysts employed by or available to it, to make a complete and unbiased analysis of the financial condition of MAI and the investment quality of its securities."

7. Continental Bank denies the allegations of paragraph 7 of Count II of the Amended Complaint, except it admits that as a senior secured creditor of MAI it received certain MAI financial information, but it denies that its officers responsible for making analyses of the financial condition of MAI and of the investment quality of MAI securities with respect to plaintiffs' funds had, or had available to them, such information for their use in making such analyses.

8. Paragraph 8 of Count II of the Amended Complaint reads:

> "8. At the time said securities were purchased by Continental and continuously thereafter, Continental failed to disclose to Plaintiffs the information that the common stock of MAI was not of an investment quality suitable for trust funds. At and during said times Continental knew or should have known but failed to disclose to Plaintiffs that MAI's financial condition was such that the market price of its common stock was inflated in relation to the operating and financial condition of the company and was subject to the risk of substantial decline. In particular, Continental knew but failed to disclose:
>
> (a) That MAI had never paid a dividend on its common stock and that there was no reasonable probability that it would do so in the foreseeable future;
>
> (b) That MAI was principally engaged in purchasing used computer and other data processing equipment from, and leasing it back to, customers on terms which did not permit the company to recover the cost of the leased equipment during the term of the lease;
>
> (c) That the business of MAI was subject to a high risk of loss on each such purchase and leaseback transaction due to the rapid rate of technological obsolescence of the leased equipment; and that, if leased equipment were to become technologically obsolete at or prior to expiration of the leased term, re-rental or liquidation of such obsolete inventory would be subject to high risk of loss; and

(d) That the price at which Continental acquired the MAI stock for Plaintiff's portfolio reflected a price-earnings ratio of approximately 50:1, which price and price/earnings ratio were excessively speculative (in relation to the high degree of risk of MAI's business) for a pension fund portfolio."

8. Continental Bank denies the allegations of paragraph 8 of Count II of the Amended Complaint, except Continental Bank admits that at the time of the purchases in question MAI had never paid a cash dividend.

9. Paragraph 9 of Count II of the Amended Complaint reads:

"9. Relying on the professional expertise of Continental, and having no knowledge of the aforesaid material information, the plaintiff Trustees acquiesced in the investment of assets of the Carpenters Pension Fund by Continental in MAI securities, and continued so to acquiesce until the sale of said securities. Relying on the professional expertise of Continental, Plaintiffs were induced to continue their relationship with Continental and were inducted not to invoke their power to terminate the aforesaid contractual relationship."

9. Continental Bank denies the allegations of paragraph 9 of Count II of the Amended Complaint, except it admits that the Trustees of Carpenters acquiesced in the investment of certain of their funds in MAI securities. Continental Bank further states that Carpenters terminated its relationship with Continental Bank on September 9, 1972.

10.-13. Paragraphs 10-13 of Count II of the Amended Complaint reads:

"10.-13. Plaintiffs adopt and reallege as if the same were set forth here in full the allegations in paragraphs 12 through 15, both inclusive, of Count 1 hereof."

10.-13. Continental Bank adopts and realleges, as though the same were set forth here in full, its answers to paragraphs 12 through 15, both inclusive, of Count I of the Amended

Complaint as its answers to paragraphs 10 through 13, both inclusive, of Count II of the Amended Complaint.

COUNT III

1.-6. Paragraphs 1-6 of Count III of the Amended Complaint read:

> "1.-6. Plaintiffs adopt and reallege as if the same were set forth here in full, the allegations of paragraphs 1 through 6, both inclusive, of Count I hereof."

1.-6. Continental Bank adopts and realleges, as though the same were set forth here in full, its answers to paragraphs 1 through 6, both inclusive, of Count I of the Amended Complaint as its answers to paragraphs 1 through 6, both inclusive, of Count III of the Amended Complaint.

7. Paragraph 7 of Count III of the Amended Complaint reads:

> "7. From and continuously after the dates of the aforesaid purchases of MAI common stock, Continental knew, but failed to disclose to Plaintiffs the information that said stock was not of an investment quality suitable for trust funds. During said time, Continental knew or should have known that:
>
> (a) During the fiscal year ending September 30, 1967, MAI suffered a decline in earnings, as compared to fiscal 1966, of more than $6 million. Net earnings were $3,219,927 in fiscal 1966; in fiscal 1967 the net loss was $3,129,156;
>
> (b) MAI suffered a net operating loss of $2,923,-293 for the fiscal year ending September 30, 1968;
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> (c) MAI incurred a special charge of $17,000,000 in fiscal 1968 to reflect the decline in valu. of obsolete inventory;
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> (d) MAI suffered net losses from operations during the fiscal years ending September 30, 1969 and September 30, 1970, of $9,823,786 and $38,405,769, respectively;

(e) The primary reason for the net losses in each of the aforesaid fiscal years was sharply declining rental revenues from unit record and other data processing equipment principally due to the technological obsolescence of MAI's equipment inventory. As the initial terms of MAI's leases expired the lessees were terminating on short notice, much of the equipment having been leased by them on a month-to-month basis, in order to obtain more technologically advanced equipment from MAI's competitors. As such equipment could not be re-rented or sold without massive losses, MAI commenced writing off said equipment with the aforesaid extraordinary charge of $17,000,000 in the fiscal year 1968 and substantially increased charges to depreciation amounting to $32,400,000 for fiscal year 1970;

(f) During fiscal year 1969, MAI prepared forecasts of projected revenue and estimated costs and expenses for the six-year period ending September 30, 1975. Based on such forecasts, it was estimated that costs and expenses would exceed revenue by approximately $8,000,000. Accordingly, a provision in that amount was charged to fiscal 1969 operations;

(g) MAI was, from a time commencing at least as early as its fiscal year ending September 30, 1968, and continuously thereafter, through at least March 31, 1971, insolvent as such term is used under the Federal Bankruptcy laws."

7. Continental Bank denies the allegations of paragraph 7 of the Amended Complaint, except it admits that the underlying information set forth in subparagraphs (c), (d), (e) and (f) is essentially correct, neither admits nor denies the underlying conclusion of law set forth in subparagraph (g), and denies that it should have "disclosed" any of such matters to Plaintiffs.

8. Paragraph 8 of Count III of the Amended Complaint reads:

"8. Notwithstanding its knowledge of the adverse and continuously deteriorating financial condition of MAI, as

aforesaid, Continental delayed and postponed selling any of said shares purchased by it for the accounts of the Carpenters Pension Fund until November, 1970, when approximately 95% of its investment had been lost."

8. Continental Bank denies the allegations of paragraph 8 of Count III of the Amended Complaint, except it admits that it sold MAI common stock for the Carpenters in November, 1970.

9. Paragraph 9 of Count III of the Amended Complaint reads:

"9. Replying on the professional expertise of Continental, and having no knowledge of the aforesaid material information, Plaintiffs acquiesced in the investment of assets of Carpenters Pension Fund by Continental in MAI securities, and continued so as to acquiesce until the sale of said securities. Relying on the professional expertise of Continental, Plaintiffs were induced to continue their relationship with Continental and were induced not to invoke their power to terminate the aforesaid contractual relationship."

9. Continental Bank denies the allegations of paragraph 9 of Count III of the Amended Complaint, except that Continental Bank admits that the Trustees of the Carpenters acquiesced in the investment of certain of their funds in MAI securities, and continued so so acquiesce until the sale of said securities. Continental Bank further states that Carpenters terminated its relationship with Continental Bank on September 9, 1972.

10.-13. Paragraphs 10-13 of Count III of the Amended Complaint reads:

"10.-13. Plaintiffs adopt and reallege as if the same were set forth here in full the allegations in paragraphs 12 through 15, both inclusive, of Count I hereof."

10.-13. Continental Bank adopts and realleges, as though the same were set forth here in full, its answers to paragraphs 12 through 15, both inclusive, of Count I of the Amended Com-

plaint as its answers to paragraphs 10 through 13, both inclusive, of Count III of the Amended Complaint.

COUNT IV

1.-8. Paragraphs 1-8 of Count IV of the Amended Complaint reads:

> "1.-8. Plaintiffs adopt and reallege as if the same were set forth here in full the allegations of paragraphs 1 though 8, both inclusive, of Count I hereof."

1.-8. Continental Bank adopts and realleges, as though the same were set forth here in full, its answers to paragraphs 1 through 8, both inclusive, of Count I of the Amended Complaint as its answers to paragraphs 1 through 8, both inclusive, of Count IV of the Amended Compaint.

9. Paragraph 9 of Count IV of the Amended Complaint reads:

> "9. Plaintiffs adopt and reallege as if the same were set forth here in full the allegations in paragraph 7 of Count III hereof."

9. Continental Bank adopts and realleges, as though the same were set forth here in full, its answer to paragraph 7 of Count III of the Amended Complaint as its answer to paragraph 9 of Count IV of the Amended Compalint.

10. Paragraph 10 of Count IV of the Amended Complaint reads:

> "10. From and after the aforesaid purchases of MAI common stock to the time of sale thereof, the interests of Continental were continuously in conflict with those of Plaintiffs, as aforesaid. During said time the financial and operating condition of MAI and its subsidiaries was known by Continental to be such that Continental was at all times obligated by virtue of its fiduciary duties to Plaintiffs to liquidate the investment of Carpenters Pension Fund in MAI common stock."

10. Continental Bank denies the allegations of paragraph 10 of Count IV of the Amended Complaint.

11. Paragraph 11 of Count IV of the Amended Complaint reads:

> "11. Nothwithstanding its knowledge and duties, as aforesaid, and because of its aforesaid conflicts of interest, Continental delayed and postponed selling any of said MAI common stock for the account of Carpenters Pension Fund in order to favor and protect its own interests over those of said Fund. Continental failed to disclose to Plaintiffs said delay and postponement and the reasons therefor."

11. Continental Bank denies the allegations of paragraph 11 of Count IV of the Amended Complaint and therefore denies that it should have "disclosed" any of such matters to Plaintiffs.

12-16. Paragraphs 12-16 of Count IV of the Amended Complaint read:

> "12.-16. Plaintiffs adopt and reallege as if the same were set forth here in full the allegations of paragraphs 11 through 15 of Count I hereof."

12.-16. Continental Bank adopts and realleges, as though the same were set forth here in full, its answer to paragraphs 11 through 15, both inclusive, of Count I of the Amended Complaint as its answers to paragraphs 12 through 16, both inclusive, of Count IV of the Amended Complaint.

COUNT V

1. Paragraph 1 of Count V of the Amended Complaint reads:

> "1. This Court has jurisdiction of this action under the doctrine of pendent jurisdiction."

1. Continental Bank denies the allegations of paragraph 1 of Count V of the Amended Complaint.

2.-13. Paragraphs 2-13 of Count V of the Amended Complaint read:

"2.-13. Plaintiffs adopt and reallege, as though the same were set forth here in full, the allegations of paragraphs 2 through 5, both inclusive, and paragraphs 7 through 14, both inclusive, of Count I hereof."

2.-13. Continental Bank adopts and realleges, as though the same were set foth here in full, its answers to paragraphs 2 through 5, both inclusive, and paragraphs 7 through 14, both inclusive, of Count I of the Amended Complaint as it answers to paragraphs 2 through 13, both inclusive, of Count V of the Amended Complaint.

14. Paragraph 14 of Count V of the Amended Complaint reads:

"14. The aforesaid conduct of Continental in creating and maintaining said conflicts of interest and failing to disclose them to Plaintiffs, as aforesaid, was a breach of its fiduciary duties to Plaintiffs, and was a breach of its aforesaid contract with Plaintiffs."

14. Continental Bank denies the allegations of paragraph 14 of Count V of the Amended Complaint.

COUNT VI

1. Paragraph 1 of Count VI of the Amended Complaint reads:

"1. This Court has jurisdiction of this action under the doctrine of pendent jurisdiction."

1. Continental Bank denies the allegations of paragraph 1 of Count VI of the Amended Complaint.

2.-5. Paragraphs 2-5 of Count VI of the Amended Complaint read:

"2.-5. Plaintiffs adopt and reallege, as though the same were set forth here in full, the allegations of paragraphs 2 through 5, both inclusive, of Count I hereof."

2.-5. Continental Bank adopts and realleges, as though the same were set forth here in full, its answers to paragraphs 2

through 5, both inclusive, of Count I of the Amended Complaint as its answers to paragraphs 2 through 5, both inclusive, of Count VI of the Amended Complaint.

6.-8. Paragraphs 6-8 of Count VI of the Amended Complaint read:

> "6.-8. Plaintiffs adopt and reallege as though the same were set forth here in full, the allegations of paragraphs 7 through 9, both inclusive, of Count II hereof."

6.-8. Continental Bank adopts and realleges, as though the same were set forth here in full, its answers to paragraphs 7 through 9, both inclusive, of Count II of the Amended Complaint as its answers to paragraphs 6 through 8, both inclusive, of Count VI of the Amended Complaint.

9.-11. Paragraphs 9-11 of Count VI of the Amended Complaint read:

> "9.-11. Plaintiffs adopt and reallege, as though the same were set forth here in full, the allegations of paragraphs 12 through 14, both inclusive, of Count I hereof."

9.-11. Continental Bank adopts and realleges, as though the same were set forth here in full, its answers to paragraphs 12 through 14, both inclusive, of Count I of the Amended Complaint as its answers to paragraph 9 through 11, both inclusive, of Count VI of the Amended Complaint.

12. Paragraph 12 of Count VI of the Amended Complaint reads:

> "12. The aforesaid conduct of Continental in purchasing said securities with knowledge of said information, and in failing to disclose said information to Plaintiffs, was a breach of its fiduciary duty to Plaintiffs, and was a breach of its aforesaid contract with Plaintiffs."

12. Continental Bank denies the allegations of paragraph 12 of Count VI of the Amended Complaint.

COUNT VII

1. Paragraph 1 of Count VII of the Amended Complaint reads:

> "1. The Court has jurisdiction of this action under the doctrine of pendent jurisdiction."

1. Continental Bank denies the allegations of paragraph 1 of Count VII of the Amended Complaint.

2.-5. Paragraphs 2-5 of Count VII of the Amended Complaint read:

> "2.-5. Plaintiffs adopt and reallege, as though the same were set forth here in full, the allegations of paragraphs 2 through 5, both inclusive, of Count I hereof."

2.-5. Continental Bank adopts and realleges, as though the same were set forth here in full, its answers to paragraphs 2 through 5, both inclusive, of Count I of the Amended Complaint as its answers to paragraphs 2 through 5, both inclusive, of Count VII of the Amended Complaint.

6.-8. Paragraphs 6-8 of Count VII of the Amended Complaint read:

> "6.-8. Plaintiffs adopt and reallege, as though the same were set forth here in full, the allegations of paragraphs 7 through 9, both inclusive, of Count III hereof."

6.-8. Continental Bank adopts and realleges, as though the same were set forth here in full, its answers to paragraphs 7 through 9, both inclusive, of Count III of the Amended Complaint as its answers to paragraphs 6 through 8, both inclusive, of Count VII of the Amended Complaint.

9.-11. Paragraphs 9-11 of Count VII of the Amended Complaint read:

> "9.-11. Plaintiffs adopt and reallege as though the same were set forth here in full, the allegations of paragraphs 12 through 14 of Count I hereof."

9.-11. Continental Bank adopts and realleges, as though the same were set forth here in full, its answers to paragraphs 12 through 14, both inclusive, of Count I of the Amended Complaint as its answers to paragraphs 9 through 11, both inclusive, of Count VII of the Amended Complaint.

12. Paragraph 12 of Count VII of the Amended Complaint reads:

> "12. The aforesaid conduct of Continental in delaying and postponing selling any of said shares with knowledge of said information, and in failing to disclose said information to Plaintiffs, was a breach of its fiduciary duty to Plaintiffs and was a breach of its aforesaid contract with Plaintiffs."

12. Continental Bank denies the allegations of paragraph 12 of Count VII of the Amended Complaint.

COUNT VIII

1. Paragraph 1 of Count VIII of the Amended Complaint reads:

> "1. This Court has jurisdiction of this action under the doctrine of pendent jurisdiction."

1. Continental Bank denies the allegations of paragraph 1 of Count VIII of the Amended Complaint.

2.-5. Paragraphs 2-5 of Count VIII of the Amended Complaint reads:

> "2.-5. Plaintiffs adopt and reallege, as though the same were set forth here in full, the allegations of paragraphs 2 through 5, both inclusive, of Count I hereof."

2.-5. Continental Bank adopts and realleges, as though the same were set forth here in full, its answers to paragraphs 2 through 5, both inclusive, of Count I of the Amended Complaint as its answers to paragraphs 2 through 5, both inclusive, of Count VIII of the Amended Complaint.

6.-9. Paragraphs 6-9 of Count VIII of the Amended Complaint read:

> "6.-9. Plaintiffs adopt and reallege, as though the same were set forth here in full, the allegations of paragraphs 7 through 10, both inclusive, of Count I hereof."

6.-9. Continental Bank adopts and realleges, as though the same were set forth here in full, its answers to paragraphs 7 through 10, both inclusive, of Count I of the Amended Complaint as its answers to paragraphs 6 through 9, both inclusive, of Count VIII of the Amended Complaint.

10. Paragraph 10 of Count VIII of the Amended Complaint reads:

> "10. Plaintiffs adopt and reallege, as though the same were set forth here in full, the allegations of paragraph 7 of Count III hereof."

10. Continental Bank adopts and realleges, as though the same were set forth here in full, its answer to paragraph 7 of Count III of the Amended Complaint as its answer to paragraph 10 of Count VIII of the Amended Complaint.

11.-12 Paragraphs 11-12 of Count VII of the Amended Complaint read:

> "11.-12. Plaintiffs adopt and reallege as though the same were set forth here in full, the allegations of paragraphs 10 and 11, both inclusive, of Count V hereof."

11.-12. Continental Bank adopts and realleges, as though the same were set forth here in full, its answers to paragraphs 10 and 11 of Count IV of the Amended Complaint as its answers to paragraphs 11 and 12 of Count VIII of the Amended Complaint.

13.-16. Paragraphs 13-16 of Count VIII of the Amended Complaint read:

> "13.-16. Plaintiffs adopt and reallege, as though the same were set forth here in full, the allegations of paragraphs 11 through 14, both inclusive, of Count I hereof."

13.-16. Continental Bank adopts and realleges, as though the same were set forth here in full, its answers to paragraphs 11 through 14 of Count I of the Amended Complaint as its answers to paragraphs 13 through 16 of Count VIII of the Amended Complaint.

17. Paragraph 17 of Count VIII of the Amended Complaint reads:

> "17. The aforesaid conduct of Continental in delaying and postponing selling any of said shares because of said conflicts of interest was a breach of its fiduciary duty to Plaintiffs and was a breach of its aforesaid contract with Plaintiffs."

17. Continental Bank denies the allegations of paragraph 17 of Count VIII of the Amended Complaint.

AFFIRMATIVE DEFENSES

1. Continental Bank states as its first affirmative defense that plaintiffs' Complaint fails to state a claim upon which relief can be granted.

2. Continental Bank states as its second affirmative defense that under the doctrine of primary jurisdiction, this Court does not have jurisdiction of the matters alleged in plaintiffs' Complaint, and that proper jurisdiction lies with the Comptroller of Currency pursuant to the National Bank Act, 12 U.S.C., § 1, et seq.

3. Continental Bank states as its third affirmative defense that pursuant to the contractual terms of the agreement between the trustees of Carpenters and Continental Bank, Continental Bank is not liable for the alleged damages to plaintiffs claimed in the plaintiffs' Complaint. The Letter of Instructions to Agent of June 6, 1958 from the Trustees of Carpenters to Continental Bank provides, in part, that:

> "In rendering these investment services, you will be acting merely in an advisory capacity, and therefore it is agreed that you shall be under no liability for any depreciation in

value of any assets held at any time in this account. It is further agreed that any action, recommendation, or comment in regard to the purchase, sale, retention or exchange of any assets of the Fund which may be taken or made by you shall be without liability on your part; . . ." (Letter of Instruction to Agent of June 6, 1958, ¶ 10.)

4. Continental Bank states as its fourth affirmative defense that the individual trustees of Carpenters approved and ratified the investment by Continental Bank of the assets of the Carpenters in the manner alleged by plaintiffs in their Complaint. The Investment Letter of Instructions to Agent of May 18, 1962 from the trustees of Carpenters to Continental Bank provided, in part, that:

> "All actions taken by you in accordance with this letter shall be ratified monthly by resolution of the Trustees at a general or special meeting and a certified copy of such resolution shall be delivered to you." (Investment Letter of Instructions to Agent of May 18, 1962.)

The trustees of Carpenters ratified each purchase of MAI stock by Continental Bank for Carpenters. In addition, plaintiffs approved and ratified the investments by Continental Bank in MAI for Carpenters by not exercising their power to remove Continental Bank as agent of Carpenters until one year after Continental Bank's sale of all MAI stock held by it for Carpenters (Letter of Instructions to Agent of June 6, 1958).

5. Continental Bank states as its fifth affirmative defense that the value of plaintiffs' pension fund appreciated during its period with the Bank, for even though the value of one stock held by the Bank for the fund may have depreciated, other securities held by the Bank for the fund appreciated in value sufficiently to more than off-set any such depreciation. Therefore, plaintiffs have not been damaged.

6. Continental Bank states as its sixth affirmative defense that the claims contained in the Complaint are barred in whole or in part by the applicable statute of limitations, pursuant to Chapter 125½ Illinois Revised Statutes, Section 137.13.

7. Continental Bank states as its seventh affirmative defense that the claims contained in plaintiffs' Complaint are barred under the doctrine of laches due to the failure of plaintiffs to assert such claims within a reasonable time after the plaintiffs knew, or should have known, the alleged facts upon which their claims are based.

8. Continental Bank states as its eighth affirmative defense that this Court does not have jurisdiction of this action because all of the Counts of plaintiffs' Complaint allege only a breach of fiduciary duty, for which jurisdiction properly lies in a state court, there being no diversity if citizenship.

9. Continental Bank states as its ninth affirmative defense that the claims in plaintiffs' Complaint in which certain alleged facts and information are alleged to have been withheld and not disclosed to plaintiffs fail to state a claim upon which relief can be granted under the Federal Securities Laws because said alleged facts and information were not "material".

10. Continental Bank states as its tenth affirmative defense the claims in plaintiffs' Complaint in which Continental Bank is alleged to have failed to disclose certain alleged facts and information to plaintiffs fail to state a claim upon which relief can be granted under the Federal Securities Laws because had such alleged facts and information been disclosed to plaintiffs, plaintiffs would not have been influenced by said alleged facts and information nor would they have relied upon said alleged facts and information.

11. Continental Bank states as its eleventh affirmative defense that this Court does not have pendent jurisdiction of Counts V through VIII of plaintiffs' Complaint, which allege only breach of fiduciary duty, there being no diversity of citizenship.

12. Continental Bank states as its twelfth affirmative defense that the claims in plaintiffs' Complaint in which Continental Bank is alleged to have had an undisclosed conflict of interest fail to state a claim upon which relief can be granted

under Federal or state law because those facts which are alleged in support of the conflict of interest allegation which are true have been general public knowledge at all times material herein.

13. Continental Bank states as its thirteenth affirmative defense that the claims in plaintiffs' Complaint in which Continental Bank allegedly failed to disclose certain alleged facts and information fail to state a claim upon which relief can be granted under Federal and state law because the alleged non-disclosure did not cause the alleged loss complained of in plaintiffs' Complaint.

14. Continental Bank states as its fourteenth affirmative defense that plaintiffs' Complaint fails to state a claim upon which relief can be granted because plaintiffs have not exercised the degree of due care and reasonable diligence which are prerequisites to recovery under Federal and state law.

15. Continental Bank states as its fifteenth affirmative defense that plaintiffs' Complaint does not state a claim upon which relief can be granted under Federal and state law because Continental Bank has acted or not acted, at all times, with complete good faith and candor, disclosing all matters which a prudent and honest trustee would disclose.

16. Continental Bank states as its sixteenth affirmative defense that Continental Bank has acted or not acted, at all times, in complete good faith, in the interest of the beneficiaries or principals of each pension fund, and with prudence and reasonable care.

17. Continental Bank states as its seventeenth affirmative defense that Continental Bank has acted, or not acted according to good business judgment, at all times material herein.

18. Continental Bank states as its eighteenth affirmative defense that the claims in plaintiffs' Complaint in which Continental Bank is alleged to have violated the Federal Securities Laws fail to state a claim upon which relief can be granted because Continental Bank did not act, or did not omit action, with the requisite degree of scienter.

WHEREFORE, defendant Continental Bank demands judgment dismissing the complaint and awarding to Continental Bank its cost and disbursements in this action.

CONTINENTAL ILLINOIS NATIONAL BANK
AND TRUST COMPANY OF CHICAGO
By its attorneys,
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BRYSON P. BURNHAM

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UNITED STATES COURT OF APPEALS

For the Seventh Circuit

Chicago, Illinois 60604

November 6, 1974

Before

Hon. LUTHER M. SWYGERT, *Chief Judge*

Hon. THOMAS E. FAIRCHILD, *Circuit Judge*

Hon. WILBUR F. PELL, JR., *Circuit Judge*

HAROLD G. O'BRIEN, BENJAMIN LIPSON, PATRICK E. GORMAN, GEORGE VEST, JR., J. J. O'DONNELL, EDWARD T. HANLEY, et al.,
Plaintiffs-Appellees,

No. 74-1671, 74-1674
74-1672, 74-1675 *vs.*
74-1673, 74-1683

CONTINENTAL ILLINOIS NATIONAL BANK AND TRUST COMPANY OF CHICAGO,
Defendant-Appellant.

Appeal from the United States District Court for the Northern District of Illinois, Eastern Division.

(72 C 2551, 660, 3132, 2935, 772, 46)

On consideration of the petition for rehearing and suggestion that if it be reheard *en banc* filed in the above-entitled cause, no judge in active service having requested a vote thereon, nor any judge having voted to grant the suggestion, and all of members of the panel having voted to deny a rehearing,

IT IS ORDERED that the petition for a rehearing in the above-entitled cause be, and the same is hereby, DENIED.

NOTE: Judge Cummings took no part in the consideration of the suggestion.

Local 734 Bakery Drivers Pension Fund Trust and Chicago District Council of Carpenters Pension Fund v. Continental Illinois National Bank and Trust Company of Chicago, a National Banking Association.

United States District Court, Northern District of Illinois, Eastern Division. Nos. 72 C 2551, 72 C 2935, 73 C 46, 73 C 660, 73 C 772, 73 C 3132.

MEMORANDUM OPINION AND ORDER

The six cases before this Court allege violations of Section 10 of the Securities Exchange Act of 1934, 15 U.S.C. §78(j) and common law claims for breach of fiduciary duties and contract. Jurisdiction is based on 15 U.S.C. § 78(aa) for the federal claims; and pendent jurisdiction is asserted as to the state law claims. Additionally, in cause No. 73 C 772, the plaintiff alleges violations of § 17a of the Securities Act of 1933, 15 U.S.C. § 77(q) and bases jurisdiction on 15 U.S.C. § 77(u). In this latter case, diversity of citizenship (28 U.S.C. § 1332) is also alleged. This Court has previously denied various motions to dismiss the claims under Rule 10b-5 and has affirmed this ruling on a motion to reconsider and to stay the proceedings pending consideration of the conflict of interest claims by the Comptroller of the Currency. The defendant bank is now before this Court on a motion for amendment of the orders of this Court dated May 10, 1974 and June 10, 1974, to include the statement specified in 28 U.S.C. § 1292(b) as a prerequisite for interlocutory appeal.

Under Section 1292(b), a District Judge in a civil action may certify an order for interlocutory appeal when he is of the opinion,

> ". . . that such order involves a controlling question of law as to which there is substantial ground for difference of opinion and that an immediate appeal from the order may

materially advance the ultimate termination of the litigation. . . ."

The defendant urges that this test has been met in the present litigation as to the issue of whether the Comptroller of the Currency has primary jurisdiction over the conflict of interest allegations in the various complaints.

Implicit in this motion is the contention that if the Comptroller of the Currency were to find that no conflict of interest existed under the national trust regulations, 12 C.F.R. 9.12, a 10b-5 action could not be maintained. As this Court noted in its prior opinion (pp. 18-19, May 10, 1974), such clearly was not the intendment of the trust regulations, *see Blaney* v. *Florida Nat'l Bank at Orlando*, 357 F. 2d 27, 30 (5th Cir. 1966). A 10b-5 claim, as well as a common law cause of action for breach of fiduciary duties, will lie regardless of any determination by the Comptroller. It is also noteworthy that the Supreme Court and several Courts of Appeals have applied 10b-5 to national banks in diverse aspects of their business, without a suggestion that any primary jurisdiction exists in the Comptroller. *See*, e.g., *Superintendent of Insurance* v. *Bankers Life and Casualty Co.*, 404 U. S. 6 (1971); *Affiliated Ute Citizens* v. *U. S.*, 406 U. S. 128 (1972); *Carroll* v. *First Nat'l Bank of Lincolnwood*, 413 F. 2d 353 (7th Cir. 1969); *Lehigh Valley Trust Co.* v. *Central Natl Bank of Jacksonville*, 409 F. 2d 989 (4th Cir. 1969). Therefore, in the opinion of this Court, there is neither a "controlling question of law as to which there is substantial ground for difference of opinion" nor will an appeal at this time "materially advance the ultimate termination of [this] litigation".

For the foregoing reasons, the defendant's motion for certification for a interlocutory appeal pursuant to 28 U.S.C. § 1292(b) is denied.

ENTER:

/s/ FRANK J. MCGARR
United States District Judge

Dated July 8, 1974

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1974

No. 74-626

CONTINENTAL ILLINOIS NATIONAL BANK AND TRUST COMPANY OF CHICAGO, *Petitioner,*

vs.

HAROLD G. O'BRIEN, ET AL., *Respondents.*

CONTINENTAL ILLINOIS NATIONAL BANK AND TRUST COMPANY OF CHICAGO, *Petitioner,*

vs.

BENJAMIN LIPSON, ET AL., *Respondents.*

CONTINENTAL ILLINOIS NATIONAL BANK AND TRUST COMPANY OF CHICAGO, *Petitioner,*

vs.

PATRICK E. GORMAN, ET AL., *Respondents.*

CONTINENTAL ILLINOIS NATIONAL BANK AND TRUST COMPANY OF CHICAGO. *Petitioner,*

vs.

GEORGE VEST, JR., ET AL., *Respondents.*

CONTINENTAL ILLINOIS NATIONAL BANK AND TRUST COMPANY OF CHICAGO. *Petitioner,*

vs.

J. J. O'DONNELL, ET AL., *Respondents.*

CONTINENTAL ILLINOIS NATIONAL BANK AND TRUST COMPANY OF CHICAGO. *Petitioner,*

vs.

EDWARD T. HANLEY, ET AL., *Respondents.*

REPLY BRIEF IN SUPPORT OF PETITION FOR CERTIORARI.

REPLY OF PETITIONER.

Continental Bank files this brief in support of its petition for certiorari and in reply to the brief filed by Respondents in opposition to that petition.*

In their brief in opposition to the petition for certiorari in these six cases, Respondents attempt to minimize the scope of the primary jurisdiction of the Comptroller of the Currency. On page 2 of their brief, they describe the issue before this Court as being the appealability of an order denying reference to the Comptroller of merely "one of multiple claims." That, however, is not the issue at all. At the heart of the complaints in these six cases is the allegation, variously phrased and often repeated, that Continental Bank was subject to a "conflict of interest" in its fiduciary role simply because it purchased for or held in the accounts of the Respondents securities of corporations to which the Bank also had extended commercial credit. Although the details of this charge are varied, it forms the focus of the present controversy (and beyond doubt presents the most difficult issue which the District Court will face in this litigation). *See* the complaint in the *Vest* case, appearing in the brief of Respondents filed in this Court, Count I, paragraphs 7, 8, 9, 10 and 11, Count IV, paragraphs 10 and 11, Count V and Count VIII. Indeed, the *only* additional issues raised by the complaints in these cases are ordinary issues of fiduciary prudence which may be readily determined upon settled legal prin-

* As a further aid to this Court, Petitioner has requested the Clerk of the Court of Appeals for the Seventh Circuit to transmit the *Brief for Appellant, Continental Illinois National Bank and Trust Company of Chicago* (filed in the Seventh Circuit) as part of the record herein in accordance with Supreme Court Rule 21(1). That brief concisely summarizes the essence of the primary jurisdiction contentions of Petitioner, and will serve to inform this Court of the importance of the underlying issue which was denied review by the Seventh Circuit. The background contained in that brief will greatly clarify the issues before this Court, and, accordingly the instant reply brief will make reference to it where necessary.

ciples. With regard to the complex claim of conflict of interest, however, *which is industry-wide in significance*, the District Court will not be able to act on an informed basis without the aid implicit in the adjudicatory powers of the Comptroller of the Currency. For a complete account of the adjudicatory powers vested in the Comptroller, and the legislative history demonstrating that Congress delegated regulation of conflicts to such administrator, *see* the Seventh Circuit *Brief for Appellant, Continental Illinois National Bank and Trust Company of Chicago*, at pages 14-24.

Respondents also assert that a decision of this Court, requiring immediate review by the Seventh Circuit of the primary jurisdiction issue raised below, would also require, by implication, interim review of a host of other orders. The contention of Petitioner, however, is not so sweeping at all. The decisions of this Court establish that appealability under 28 U.S.C. § 1291 requires consideration of a number of criteria including the "collateral" nature of the order subject to appeal, the settled or conclusive nature of that order, the importance and difficulty of the order, the fundamentality of the order to further proceedings in the District Court, and the measure of injury resulting from delayed review. *See* Petition for Certiorari, pages 11-14.

In a footnote on page 3 of their brief, Respondents attempt to diminish the analysis of Petitioner as to the injuriousness of the "conflict" theory of the complaints herein by labelling such analysis an "in terrorem" argument. The true significance of this litigation, however, and its implication for the nation's commercial banks, is aptly summarized in *Problems of Fiduciaries under the Securities Laws*, a report composed by two section committees of the American Bar Association, and appearing in the A.B.A. *Real Property, Probate and Trust Journal*, Vol. 9, No. 3 (Fall 1974):

> "The 'inherent conflict' theory of the claims in *O'Brien* and *O'Donnell* [two of the six cases here], if successful . . . might well make the maintenance of commercial relation-

> ships with, and investments by a trust department in, the same corporate customer impractical if not impossible. The commercial relationships normally maintained by any large bank are so extensive that to bar trust department investments in securities issued by commercial banking customers would significantly reduce the number of issues of substantial, widely held corporations available for investment. This, in itself, might require curtailment of the activities of either the commercial department or the trust department with respect to this particular issuer or its securities. The practical consequences might well be equivalent to the divestment of the trust department, a result criticized above." Id. at 301-302.*

"Divestment," of course, as threatened by the basic theory of this litigation, would uproot the major premise on which Congress acted in 1913 when it united trust and commercial functions in National Banks. *See* the Seventh Circuit *Brief for Appellant, Continental Illinois National Bank and Trust Company of Chicago,* pages 14-18, 29-35.

In the footnote on page 6 of their brief in opposition here, Respondents seek to show the inapplicability of the primary jurisdiction doctrine by citing a number of decisions which adjudicated claims against a variety of banks without prior reference to any administrative agency. The *non sequitur* advanced, however, is quite apparent. It suffices to say that in *none* of the cited cases was the primary jurisdiction doctrine invoked. In none of these cases was a basic issue involved—such as the present "conflict of interest" issue—which fell squarely within the adjudicatory competence of a bank regulatory agency, which was specifically delegated to that agency by Congress, and which vitally affected financial institutions subject to the jurisdiction of the agency across the entire nation. The citation by Respondents of cases such as these is equivalent to citing a

* The Report states at the outset that "the views expressed here are those of a consensus of the committees described in this report . . ." One of the individuals participating in the work of the committees was Robert Curley, a securities lawyer from Mayer, Brown & Platt, the law firm which serves as counsel for Petitioner herein. *See* Report at pages 292-93.

string of antitrust decisions, in which no primary jurisdiction question was ever raised, to support the erroneous proposition that the primary jurisdiction doctrine is never applicable in antitrust litigation.

On pages 7-10 of their brief, Respondents maintain that the order subject to appeal in these six cases is not reviewable under 28 U.S.C. § 1291 because denial of immediate review will occasion no injury. That, however, is simply not true. The cases here involved are extraordinary in dimension, several of them involving broad classes of plaintiffs under rule 23, F.R. Civ. P. They are already six in number, and a seventh action raising identical issues has recently been filed and assigned to Judge McGarr in the District Court below. It is obvious that a tremendous sacrifice of judicial time and private resources is threatened if these cases lumber ahead, without clarification of the primary jurisdiction question raised below, and without correction of the reversible error occurring at the outset. Moreover, by failing to refer these cases to the Comptroller of the Currency, the District Court has interfered with the regulation of the expert administrator over a pervasively supervised industry. The importance of immediate review is underscored by the grave uncertainty which these suits have engendered throughout the banking industry, an uncertainty casting suspicion upon the most orthodox of commercial and fiduciary practices. *See* the joint report of the A.B.A. committees cited above, *Problems of Fiduciaries Under the Securities Laws, A.B.A. Real Property, Probate and Trust Journal*, Vol. 9, No. 3 (Fall 1974), pages 300-302. The conflict question here raised should be clarified promptly through the expert assistance of the bank regulator deputized by Congress to oversee the industry involved.

This Court has on three occasions stressed the importance of immediate review to correct lower court decisions which erroneously restrict the administrative jurisdiction of a federal agency. This Court has thus acknowledged the magnitude of the injury involved and the need for prompt correction. *See Local No. 438 Construction & General Laborers' Union* v. *Curry*, 371